



STATE OF WISCONSIN
Department of Employee Trust Funds
David A. Stella
SECRETARY

801 W Badger Road
PO Box 7931
Madison WI 53707-7931
1-877-533-5020 (toll free)
Fax (608) 267-4549
<http://etf.wi.gov>

CORRESPONDENCE MEMORANDUM

DATE: February 15, 2011

TO: Deferred Compensation Board

FROM: Shelly Schueller, Director, Deferred Compensation Program
David H. Nispel, General Counsel

SUBJECT: Securities and Exchange Commission "Pay to Play" Regulations and the Wisconsin Deferred Compensation Program

This memo is for informational purposes only. No Board action is required at this time.

We are writing to inform you about federal rules that pertain to the investment options offered through the Wisconsin Deferred Compensation Program (WDC). We also want to inform you about action the Department of Employee Trust Funds (ETF) has taken to date in response to these rules. The federal rules address the practice commonly referred to as "pay to play," which is the practice of making campaign contributions to officials in order to influence the process of awarding contracts for the management of public pension plan assets and other governmental investments.

In July 2010, the Securities and Exchange Commission (SEC) adopted a new rule under the Investment Advisers Act of 1940 that restricts political contributions to elected officials or candidates by investment advisers. The SEC also adopted rule amendments requiring a registered adviser to maintain records of political contributions made by the adviser or certain of its executives or employees. Investment advisers must be in compliance with the rule as of March 14, 2011. Advisers to registered investment companies that are covered investment pools must comply with the rule by September 13, 2011.

For purposes of this memorandum, the new rule and amended rule simply will be referred to as "the rule." A summary of the rule follows. Also, we have attached definitions of several of the key terms used in the rule.

Reviewed and approved by Anne Boudreau, Deputy Administrator,
Division of Retirement Services

Signature

Date

02-16-2011

| Board | Mtg Date | Item # |
|-------|----------|--------|
| DC | 03.01.11 | 6 |

The rule applies to investment advisers that have government clients or manage assets of a government entity through a pooled investment vehicle that is an investment option of a participant directed plan or program of a government entity, such as a s. 457 plan like the WDC. The rule also applies to any of the investment adviser's executive officers, supervisors and certain employees who solicit a government entity. Similar pay to play restrictions also apply to third-party agents and solicitors.

Advisers and covered associates are prohibited from taking any action which, if done directly, would result in a violation of this rule. Accordingly, indirect payments or contributions made to any official of a government entity by an adviser or its covered associates or by a third party (such as consultants, attorneys, family members, friends or companies affiliated with an adviser) are prohibited.

There is a de minimus exception in the rule. A covered associate may make a total contribution of up to \$350 per election to an official, if the contributor is entitled to vote for the official. If the covered associated is not entitled to vote for the official, then a contribution of up to \$150 per election may be made.

Registered investment advisers that have government clients or provide investment advisory services to a covered investment pool are required to maintain certain records that will allow the SEC to examine for compliance with the rule. Advisers to covered investment pools must make and keep a list of government entities that invest, or have invested in the past five years, in a covered investment pool. That list must include any government entity that selects a covered investment pool to be an option of a plan or program of the entity, such as a s.457 plan.

Compliance with the SEC rule does not fall upon the WDC, the Deferred Compensation Board, or ETF, but rather on the investment options. The penalties for non-compliance are serious. If an adviser violates the rule, the adviser is prohibited for a two-year period from receiving compensation from a government entity for which it provides advisory services or management services either directly or through a covered investment pool.

After reviewing the new rules, ETF contacted each of the investment options for the WDC and requested that they inform ETF in writing what action, if any, they have taken or intend to take to comply with these rules. As shown in the table below, the WDC's investment option providers are familiar with the new rules, have or are in the process of adopting new policies and expect their employees to comply with them.

| Investment Firm | Adopted New Policies/ Procedures | Company Political Contribution Limit | Contribution Recordkeeping |
|-----------------------------------|---|--|-----------------------------------|
| Calvert | Yes | Requires prior clearance and \$250 per person limit in household | Yes |
| Capital Guardian (American Funds) | Yes, including internal education | Requires prior clearance | Yes |
| Dimensional | Yes – will be amended | Did not directly address/respond | Did not directly address/respond |
| Federated | Yes | Requires prior clearance | Yes |
| Galliard | Yes | Requires prior clearance | Yes |
| Schwab * | | | |
| T. Rowe Price | Yes | Requires prior clearance | Yes |
| Vanguard | Yes | In development – will require prior clearance | Yes |

* Request to Schwab was "elevated" internally; response pending but not yet available.

Three of the WDC's investment providers, Fidelity, M&I Bank and BlackRock, have stated that they are exempt from the new rules. Fidelity, M&I Bank and BlackRock responded to our inquiry with letters indicating that they are not subject to the Investment Advisors Act of 1940; Fidelity because they consider themselves a broker dealer and M&I Bank and BlackRock because they are banking associations/holding companies. Fidelity did note that certain of their affiliated investment advisors (example: Pyramis Global Advisors) are subject to the new rule and consequently the company will be taking steps to make sure they are in compliance with all requirements.

We will be available at the Board meeting to discuss this memo with you and answer any questions.